

# Aviation in a post-pandemic world: challenges and opportunities

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It is difficult to imagine a world without flying. That's precisely what happened in March this year, when the aviation industry was sent into a tailspin following the outbreak of COVID-19, as airports, air spaces and borders were shut down, and most fleets were grounded. The industry has been among the worst hit by the pandemic, with many airlines forced to suspend or close operations over the past eight months, disrupting supply chains globally and claiming millions of jobs.

The aviation sector has suffered in a couple of distinct ways. First, there is a fear of contagion. Few other businesses require such proximity with strangers for hours, while potentially carrying the infection from one geography to another. Second, in midst of the worst economic downturn in recent history, there has been a sharp decline in travel across the spheres of business and tourism. With no immediate cure or vaccine in sight, the pandemic will likely continue to challenge our normal lives and air travel in particular.

Aviation contributes nearly 4 per cent of the global gross domestic product (GDP) and supports more than 65 million jobs around the world<sup>1</sup>. Had 2020 been a normal year, it would have seen more than 40 million commercial flights take to the skies carrying more than 4.7 billion passengers and 65 million tons of cargo<sup>2</sup>.

The fallout has been unprecedented, with the consequences for the industry already much worse than anything witnessed in recent history including the aftermaths of 9/11, SARS, the global financial crisis and the volcanic eruption in Iceland which disrupted normal air travel for a short period in some parts of the world. The travel and tourism industry is expected to lose more than USD1 trillion in revenues this year<sup>3</sup> and close to 200 million jobs<sup>4</sup>, considering the impact not just on business travel but on global tourism as well. The International Air Transport Association (IATA), Airport Council International (ACI) and International Civil Aviation Organisation (ICAO), the three principal representatives and custodians of the aviation industry globally, predict that the sector will take at least three to four years to roll back to 2019 levels<sup>5</sup>. The recovery is expected to be slow, uncertain, and inevitably, painful.

However, from overt despair a quarter ago, we are now seeing green shoots of progress, and the recovery in many regional aviation markets has triggered cautious optimism among investors, governments and regulators on future prospects, especially in countries with strong domestic markets such as India, China, Indonesia and the European Union.

India, in particular, has done well to bring back flyers on domestic routes while international passenger services continue to be restricted and operated under 'travel bubbles' through bilateral agreements with partner countries. Interestingly, the air cargo market has continued to grow steadily to meet the increasing demand for food essentials and medical aid. The fall in passenger demand has also prompted

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many carriers to retrofit aircraft to carry more cargo across borders, in search of better margins and cash flows.

As with any major crisis, COVID-19 and its economic ramifications have presented both challenges and opportunities. Let's briefly examine five key challenges that the industry faces as it strives to recover from its precipitous fall.

1. **Rationalisation of corporate travel** - Even as markets recover, the increasing adoption of technology and work-from-home routines are likely to reduce demand for business travel significantly. Some experts estimate this to be higher than 40 per cent<sup>6</sup>, as employees and traditional jetsetters become more comfortable with better and cheaper technology and hybrid workspaces. The need to conserve cash and reduce costs in the long run will reinforce such behaviours as businesses struggle to restore profitability and value for shareholders. Airlines and airports will have to contend with this new normal, innovate and rejig their growth strategies accordingly.
2. **Drop in commercial revenues** - The need for social distancing and personal hygiene while travelling has already hurt passenger spends within terminals significantly. Commercial or non-aeronautical revenues are a rich source of income in airports businesses, more than 50 per cent of overall revenues in many mature airports<sup>7</sup>, a large proportion generated by duty-free retail, which has completely dried up with limited or absent international footfalls. Job losses, rationalisation of salaries, reduced economic growth and lower disposable incomes are likely to exacerbate the impact in the future reducing footfalls and spends both at airports and in-flight. Airport owners will need to transform their commercial business and operating models to deal with this new reality but will be helped by advances in technology and the growing popularity of digital platforms.
3. **Market distortions** – Airlines have suffered heavy losses in revenue from the pandemic, threatening the survival of many, especially given the nature of the business (high capex, cash guzzling, low margins, and with long paybacks). Financially solvent governments (U.S., Germany, Singapore, U.A.E., Japan among others) have stepped in to provide relief to many national carriers through grants, soft loans, credit guarantees and other forms of support<sup>8</sup>. Private carriers have not been equal beneficiaries in such markets with minimal or no support at all from regulators or governments potentially jeopardising competitive tension and aggravating market distortions that can impact both choice and fares for flyers in the future.
4. **Impact on future investments and asset rebalancing** - High growth markets like India have created capacity to meet consistently growing demand for air travel over the last two decades. In some airports, capacity has either been built upfront or being created with significant costs already incurred. While the long-term outlook for growth remains strong in underpenetrated air markets like India, the next three to four years are going to pose significant challenges for

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airport owners and investors to monetise assets or repurpose them to create shareholder value. In some cases, competition from newer asset-light airports may also pose an additional challenge on asset rebalancing and profitability.

- 5. The double whammy for regulators** - A combination of factors, such as weak demand outlook, poor revenues, high asset servicing costs and low liquidity, appears to have caught regulators across the world in a perfect storm. Compensating airports on current business models without imposing an additional pricing burden on airports' principal users- airlines, passengers, commercial businesses - presents a major conundrum for regulators. In some cases, they also must make difficult decisions in fairly and equitably reallocating airport assets such as slots and real estate.

No crisis, as the adage goes, should be allowed to go waste. The impact of COVID-19 on the aviation sector has been severe but it has also provided an opportunity for the industry to reimagine its future. Here are five ways in which it could be done.

- 1. Refocus on the cost-line** - Innovations in design, technology and financing can significantly change the cost of providing services for both airlines and airports. It can help deliver more bang for the buck and cushion the pressure on both affordability and profitability. Solar powered airports, electric bussing, green buildings and recycling can engender significant savings in operating costs and could become the norm for the best performing airports.
- 2. Make technology work harder for you** - In a progressively digital world, bytes carry more value than bricks if used well. Investing in the right tools and technology can not only help monetise assets better but also significantly improve operating efficiency and customer experience.
- 3. Transform the operating model** - Technology can facilitate a complete revamp of the operating model for greenfield assets. For example, touchless check-ins, RFID bag-tags, contactless and paper-less immigration and boarding processes can largely obviate the need for large passenger concourses and check-in areas and release more monetisable commercial spaces. Sustainability is a concomitant theme that can enhance asset productivity and unlock value by effectively managing life-cycle costs. Another important consideration would be to find the right balance between resilience and efficiency.
- 4. Collaborate** - Airlines and airports have often been adversaries in a commercial ecosystem but may have a lot to gain from each other in a demand-constrained, price-sensitive market. Sharing data could be the key to maximising value and sharing gains from mutual benefits. It could not only help extend the clientele beyond airport boundaries but also help optimise costs while providing more value for passengers and airport users.

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- 5. Innovate** - History has shown us that crises have often spawned the best inventions and innovations. The immense value of data and technology that we have access to today cannot be overstated. They act as perfect levers to invent and innovate solutions that can boldly take on a world shaped by volatility, uncertainty, complexity and ambiguity (VUCA). Will we see more bio-fuelled planes? Will we have more satellite-based navigation systems? Can we have integrated departure and arrival areas in a digitally enforced airport?

The aviation industry has repeatedly shown the resilience to come back stronger, bolder and smarter from previous crises that have threatened to disrupt the status quo. There is a need for a sharp, rational and consistent approach to reforms to help the industry cruise at a newer and higher altitude and redefine its new normal. The changing geo-political scenario and impending power shifts globally also demand a swift and adroit approach. Expedient policy changes will be required to exploit the opportunity, accrete strategic gains and create a better future.

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<sup>1</sup> Air transport supports 65.5 million jobs and \$2.7 trillion in economic activity, International Air Transport Association (IATA), 2 October 2018

<sup>2</sup> After Challenging Year, Improvement Expected for 2020, IATA, 11 December 2019

<sup>3</sup> Impact assessment of the COVID-19 outbreak on international tourism, UN World Tourism Organization (UNWTO), May 2020

<sup>4</sup> World Travel & Tourism Council (WTTC) research, June 2020

<sup>5</sup> ACI Advisory Bulletin, Airports Council International (ACI), 31 August 2020

<sup>6</sup> Business travel recovery survey, The Institute of Travel Management, September 2020

<sup>7</sup> Airports see uptick in retail sales, line up sweeteners for passengers, Business Standard, 14 October, 2020

<sup>8</sup> Crippled Airline Industry to Get \$25 Billion Bailout, Part of It as Loans, New York Times, Apr 29, 2020; Japanese airline group seeks \$18 billion in government aid, Nikkei Asian Review, April 6, 2020; Singapore Airlines latest to get massive rescue amid coronavirus crisis, Reuters News, March 27, 2020; Lufthansa agrees €9bn bailout with German government, the Guardian, May 26, 2020; Dubai vows to support Emirates as global airlines race for cash, the Financial Times, March 31, 2020

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